



## AUDIT OF OUT-OF-STATE PURCHASES

**From The Office Of State Auditor  
Claire McCaskill**

*Agency personnel followed state statutes in awarding contracts to out-of-state vendors; however, the Office of Administration needs to establish procedures to identify and report out-of-state purchases.*

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PERFORMANCE AUDIT



Office of  
Missouri State Auditor  
Claire McCaskill

September 2004

### **Oversight and Management of Out-Of-State Purchases**

The Office of Administration (OA) and other state agencies followed statutory guidance in making out-of-state purchases. However, the OA has not established procedures to effectively identify or monitor out-of-state purchase activity.

#### **No adequate method to identify out-of-state purchases**

During 2003, OA estimated 30 percent of fiscal year 2003 procurements were made to out-of-state vendors. However, auditor analysis shows no more than 14 percent of the \$2.4 billion in purchases would have represented out-of-state purchases. The higher percentage estimated by OA is the result of using vendor billing addresses. Although OA plans to report on these purchases, as of April 2004, procedures had not been established to accurately identify and report out-of-state purchases. (See page 4)

#### **OA taking steps to enhance in-state purchases**

In response to the Executive Order 03-27, requiring Missouri preference, OA developed guidance for state agencies. This guidance includes a decision matrix to be used in applying executive order requirements and was distributed to state agencies in April 2004. (See page 5)

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# **AUDIT OF OUT-OF-STATE PURCHASES**

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**CLAIRE C. McCASKILL**  
**Missouri State Auditor**

Honorable Bob Holden, Governor  
and  
Jacquelyn D. White, Commissioner  
Office of Administration  
Jefferson City, Missouri 65102

State agencies spent \$2.4 billion in fiscal year 2003 on goods and services, and capital improvements, from in-state and out-of-state vendors. Because of the importance of ensuring Missouri vendors have adequate opportunities to be considered for state purchases, we focused audit efforts on determining whether improvements are needed in the management and oversight of out-of-state purchases. Audit objectives included determining whether (1) the Office of Administration (OA) and other state agencies complied with statutory guidance in making out-of-state purchases, (2) improvements in identifying out-of-state purchase activity are needed, and (3) the state has taken action to enhance opportunities to buy goods and services from Missouri vendors.

We found purchase personnel complied with statutory guidance in purchasing and/or awarding contracts for goods and services, and capital improvements for 128 sampled payments reviewed. The sampled payments totaled \$29 million.

We also found OA had not established procedures to identify and report out-of-state purchase activity. During 2003, OA estimated out-of-state purchases represented 30 percent of total purchases. However, our analysis showed out-of-state purchases represented no more than 14 percent, or \$333 million of \$2.4 billion in purchases during fiscal year 2003.

The state has taken action to enhance competitive opportunities for Missouri vendors. Executive Order 03-27, issued in December 2003, allowed state agencies operating under Chapter 34 RSMo purchase guidelines, to consider the economic impact of purchasing Missouri products. In response, OA developed guidance for agency use in implementing the executive order and distributed it to state agencies in April 2004.

We conducted our audit in accordance with applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and included such tests of the procedures and records as were considered appropriate under the circumstances.

A handwritten signature in black ink, reading "Claire McCaskill". The signature is fluid and cursive, with the first name "Claire" and last name "McCaskill" clearly distinguishable.

Claire McCaskill  
State Auditor

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## **RESULTS AND RECOMMENDATIONS**

### **Oversight and Management of Out-of-State Purchases Has Been Adequate**

The Office of Administration (OA) and other state agencies followed statutory guidance in making out-of-state purchases. While purchase personnel followed statutory guidance, which requires them to award contracts and purchases to the lowest and best bidder regardless of location, OA has not established procedures to identify out-of-state purchase activity. As a result, OA has no mechanism to monitor out-of-state purchase activity. The state has taken action to enhance competitive opportunities for Missouri vendors. Executive Order 03-27 allows state agencies, operating under Chapter 34 RSMo purchasing guidelines, to consider the company's economic presence within the State of Missouri (e.g., type of facilities: sales offices; sales outlets; divisions; manufacturing; warehouse; other), including Missouri employee statistics. In response to the executive order, OA developed guidance implementing the executive order and distributed it to state agencies in April 2004.

### **Background**

State agencies spent \$2.4 billion in fiscal year 2003 on goods and services, and capital improvements from in-state and out-of-state vendors. OA's Division of Purchasing and Materials Management is responsible for the purchase of all state required supplies, materials, equipment and professional or general services, in accordance with Chapter 34 RSMo, except for those agencies exempted by law.<sup>1</sup> Chapter 34 states purchases in excess of \$3,000 shall be awarded to the lowest and best bidder. It also states agencies shall give preference to Missouri products and firms when the quality is equal or better and the delivered price is the same or less than out-of-state vendors. The preference applies to businesses or individuals maintaining offices or places of business in the state.

OA's Division of Design and Construction is responsible for the design, construction, renovation and repair of state facilities, and reviews all requests for appropriations for capital improvements in accordance with Chapter 8 RSMo (excludes highway and bridge projects of the Missouri Department of Transportation). Chapter 8 states contracts for construction projects shall be awarded to the lowest bidder and preference shall be given to products of mines, forests, and quarries located in the state when found in marketable quantities. Purchases for architectural, engineering, and land surveying services are awarded on the basis of demonstrated competence and qualifications at fair and reasonable prices.

### **Methodology**

We reviewed applicable state statutes, federal regulations, and agency purchasing policies and procedures, and sampled 299 payments from Statewide Advantage for Missouri II (SAM II) identified as payments to out-of-state vendors, to determine whether agencies complied with applicable guidance in awarding contracts to out-of-state vendors. To determine whether

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<sup>1</sup>Agencies exempt from Chapter 34 RSMo include the Legislative Branch, Judicial Branch, Lottery Commission and Department of Transportation (except data processing, telecommunications, and printing). Exempt agencies follow other state statutes, federal regulations or agency purchasing policies.

improvements were needed in identifying out-of-state purchase activity, we reviewed OA's procedures used in identifying out-of-state purchase activity and compared OA's estimate to sample results. We also reviewed OA guidance issued to state agencies relating to Executive Order 03-27 and interviewed OA personnel to determine what actions are being taken to enhance opportunities for Missouri vendors.<sup>2</sup>

### **State agencies complied with statutory guidance in making out-of-state purchases**

OA and other state agencies complied with statutory guidance in purchasing and/or awarding contracts for goods and services, and capital improvements to out-of-state vendors for 128 sampled payments reviewed by auditors. The sampled payments totaled \$29 million. Purchase personnel followed Chapter 34 RSMo and Chapter 8 RSMo, or other applicable guidance. See page 3 for additional information on statutory guidance.

### **OA has not developed an adequate method to identify out-of-state purchases**

During 2003, OA estimated 30 percent of fiscal year 2003 procurements were made to out-of-state vendors. An OA official stated OA personnel used vendor billing addresses shown in SAM II to formulate this estimate.

OA estimate of out-of-state purchases is not accurate

Our analysis of out-of-state vendors shows no more than 14 percent of \$2.4 billion in purchases, made during fiscal year 2003, would have represented out-of-state purchases. The dollar universe from which our sample was selected was \$577 million for fiscal year 2003. The 299 payments in our sample were paid to 161 vendors. Those vendors received total payments of \$372 million in fiscal year 2003. By verifying addresses for the vendors, we determined \$244 million of the \$372 million represented in-state purchases. Consequently, as much as \$333 million (\$577 million - \$244 million), or 14 percent of fiscal year 2003 purchases (\$333 million / \$2.4 billion) could have been paid to out-of-state vendors.<sup>3</sup>

As of April 2004, procedures had not been established to accurately identify and report out-of-state procurements. However, an OA official stated the long term goal is to track and report out-of-state procurements on a quarterly basis for management's use.

All state procurements are entered in SAM II by agency data entry personnel. Vendor data entered includes the vendor's billing address. SAM II is equipped with an "in-state" indicator field, however, completion of this field is not a requirement but could be used to account for in-state and out-of-state procurements.

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<sup>2</sup> See Appendix I, page 7, for objectives, scope and methodology.

<sup>3</sup> Since we did not test the balance of \$205 million in the \$577 million universe, any occurrence of in-state purchases within the \$205 million would reduce the 14 percent we reported as out-of-state purchases.

## **OA taking steps to enhance in-state purchases**

In December 2003, the governor issued Executive Order 03-27, which directed OA to ensure all state agencies follow the requirements of this executive order and the Missouri preference provisions set forth in Chapter 34, RSMo.<sup>4</sup> In response, OA developed guidance which provides a summary of the executive order and a decision matrix to be used in applying executive order requirements. OA distributed it to state agencies in April 2004.<sup>5</sup>

The executive order requires state agencies to make a good faith search for, and purchase, Missouri products. It also states OA and other state agencies may consider the economic impact of products generated by Missouri vendors to the state. In addition, OA must provide a listing of Missouri products to all interested parties and state agencies and make efforts to identify and give notice of bidding opportunities to Missouri manufacturers or service providers. To help Missouri vendors improve products and services, to meet the needs of state government and become more competitive, the executive order requires state departments to prepare written explanations of why vendors did not receive awards, if requested by Missouri bidders.

When economic impact factors are to be considered, OA's guidance requires contractors to address the following in responding to agency requests for bids and proposals:

1. A description of the proposed services that will be performed and/or the proposed products that will be provided by Missourians and/or Missouri products.
2. A description of the economic impact returned to the state of Missouri through tax revenue obligations.
3. A description of the company's economic presence within the state of Missouri (e.g., type of facilities: sales offices; sales outlets; divisions; manufacturing; warehouse; other), including Missouri employee statistics.

The guidance also requires the agencies to evaluate these factors.

## **Conclusions**

OA and state agency personnel followed statutory guidance in purchasing and/or awarding contracts for goods and services, and capital improvements to out-of-state vendors. However, OA has not established procedures needed to accurately identify out-of-state purchase activity. As a result, OA has no mechanism to monitor and report out-of-state purchases. OA plans to report on these purchases; however, at the conclusion of our review, procedures had not been established to accomplish this task. Tracking out-of-state purchase activity could be a useful management tool.

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<sup>4</sup> See Appendix III, page 10, for the executive order.

<sup>5</sup> See Appendix IV, page 12, for OA's guidance.



## **Recommendation**

We recommend the Commissioner of OA:

Establish policies and procedures requiring state agencies to identify in-state and out-of-state vendors and monitor the results.

## **Office of Administration Comments**

*There are over 156,000 business-type vendors in the SAM II Financial system and the method utilized by the State Auditor's Office for determining a Missouri business (161 vendors checked) was extremely time consuming. The recommendation requires the agencies to identify in-state and out-of-state vendors. However, since vendors can also self-register through DPMM's website, the on-line vendor registration system would have to be modified so vendors could appropriately identify themselves as a Missouri business. OA will determine the feasibility of establishing policies and procedures needed to track out-of-state purchases.*

## **OBJECTIVES, SCOPE AND METHODOLOGY**

### **Objectives**

Our objectives included determining whether (1) OA and other state agencies complied with statutory guidance in making out-of-state purchases, (2) improvements are needed in identifying out-of-state procurement activity, and (3) enhanced opportunities exist to buy goods and services from Missouri vendors.

### **Scope and Methodology**

We reviewed Statewide Advantage for Missouri II (SAM II) expenditures<sup>1</sup> related to the purchase of goods, services and capital improvements for fiscal year 2003, and identified \$2.4 billion in purchase activity. We also interviewed OA and other agency personnel at selected agencies.<sup>2</sup>

To test whether decisions to buy from out-of-state vendors complied with state statutes, we also conducted a statistical sample of payments made to vendors. To determine the sample universe of payments made to out-of-state vendors, we first used vendor billing addresses shown in SAM II which resulted in a sample universe of \$577 million. Using a 95 percent confidence level, a population of \$577 million, and a materiality level<sup>3</sup> of \$5.8 million (1 percent), resulted in a sample of 299 payments. We used monetary unit sampling to determine a sample selection interval of \$1.9 million<sup>4</sup> after haphazardly selecting the first monetary unit of about \$255,000 without any consideration as to which sample item would be selected.

To determine whether vendors were located in-state or out-of-state, we reviewed 161 vendors that had received 299 sampled payments totaling \$78 million to verify whether vendors were actually located in-state or out-of-state. When not readily apparent, we contacted vendors to determine whether vendors maintained Missouri offices or places of business. We then classified the vendor as an in-state vendor, and did not conduct any further audit work, or an out-of-state vendor. For vendors classified as out-of-state, we reviewed contracts and bid documentation, if applicable, for sampled payments to determine whether related purchases had been made in accordance with statutory and/or agency guidance. For payments related to purchases not requiring competitive bids,<sup>5</sup> we interviewed agency and/or procurement personnel and reviewed the rationale for using an out-of-state vendor.

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<sup>1</sup> Object codes are used to categorize state expenditures. OA Division of Accounting personnel identified applicable object codes related to the purchase of goods, services, and capital improvements for fiscal year 2003.

<sup>2</sup> See Appendix II, page 9, for listing of agencies reviewed and contacted.

<sup>3</sup> The materiality level specifies the amount of money considered significant and is the maximum amount of error auditors were willing to accept in the population without detection.

<sup>4</sup> We accumulated \$1.9 million in payments before selecting the next sample item.

<sup>5</sup> According to Chapter 34 RSMo, purchases less than \$3,000 do not require competitive bids.

## **APPENDIX I**

To determine if adequate procedures exist to identify out-of-state procurement activity, we discussed the method used by OA personnel to estimate the extent of out-of-state procurements and compared OA's estimate to the results achieved through our sample.

To determine whether the state has taken action to enhance competitive opportunities for Missouri vendors, we held discussions with OA officials and reviewed OA guidance issued to state agencies relating to a December 2003 executive order.

To determine the reliability of computer generated data, we traced data elements from our sample of 299 payments to corresponding information in SAM II. The test disclosed no errors.

We conducted our review from December 2003 to April 2004.

**AGENCIES AND OUT-OF-STATE PAYMENTS REVIEWED**

Of the 299 sampled payments, we determined 128 payments totaling \$29 million had been made to out-of-state vendors during fiscal year 2003. Table II.1 displays 15 agencies associated with sampled payments related to out-of-state procurements.

**Table II.1: Out-of-State Purchases Reviewed by Agency**

<b>Agency/Department</b>	<b>Number of Payments</b>	<b>Total Amount</b>
Conservation <sup>1</sup>	3	\$ 297,995
Corrections <sup>1</sup>	17	418,798
Economic Development	2	19,192
Elementary and Secondary Education	8	5,504,508
Health	2	79,945
Higher Education	6	1,478,941
Judiciary <sup>1</sup>	2	11,802
Mental Health <sup>1</sup>	2	70,379
Natural Resources	3	276,376
OA <sup>1</sup>	2	32,621
Public Defender <sup>1</sup>	1	2,100
Public Safety	7	2,712,615
Revenue <sup>1</sup>	10	3,376,001
Social Services <sup>1</sup>	8	407,876
Transportation <sup>1</sup>	55	14,313,268
<b>Total</b>	<b>128</b>	<b>\$29,002,417</b>

<sup>1</sup> OA did not have procurement data so auditors contacted agency.

Source: SAM II and SAO analysis.

**EXECUTIVE ORDER 03-27**

WHEREAS Missouri business and workers are highly skilled and efficient and produce high quality products and services.

WHEREAS, the economy of the State of Missouri benefits from keeping Missouri tax dollars in the state when state government purchases these excellent Missouri products and services. Taxpayers should expect to realize the full value for every tax dollar spent in Missouri.

WHEREAS, product and service specifications contained in an offer for a Missouri purchasing bid continue to provide free and open competition for all vendors, including those vendors offering Missouri products and services.

WHEREAS, the State of Missouri should purchase goods and services from in-state companies whenever possible in order to support Missouri business, grow the Missouri economy, and provide jobs for Missouri workers.

NOW, THEREFORE, I, BOB HOLDEN, GOVERNOR OF THE STATE OF MISSOURI, by virtue of the authority vested in me as governor of the State of Missouri, do hereby order as follows:

1. For purposes of this executive order, the term "Missouri product" refers to goods or commodities, which are manufactured, mined, produced or grown by companies in Missouri, or services provided by such companies in Missouri.
2. Under Sections 34.040 and 34.042, RSMo, a Missouri state government purchaser shall purchase a product that is determined to be the "lowest and best." In addition, Sections 34.070 and 34.073, RSMo, authorize a preference for Missouri products.
3. In determining the lowest and best award, cost and other factors are considered in the evaluation process. Factors may include value, performance and quality of a product.
4. Missouri state government agencies shall purchase a Missouri product unless it is determined that the value (including, but not limited to price, performance, and quality) of the Missouri product does not meet the needs of the user.
5. In assessing value, the Commissioner of the Office of Administration and other Missouri state governmental purchasers may consider the economic impact to the State of Missouri for Missouri products versus the economic impact of products generated from out of state. This economic impact may include the revenues returned to the state through tax revenue obligations.
6. The Commissioner of the Office of Administration shall provide a listing of Missouri products and access to such listing to all state government agencies and other interested

### **APPENDIX III**

parties. The Commissioner of the Office of Administration shall also make efforts to identify and give notice of state government bidding opportunities to Missouri manufacturers or service providers. Finally, the Commissioner of the Office of Administration shall ensure state agencies follow the requirements of this Executive Order and the Missouri preference provisions set forth in Chapter 34, RSMo.

7. State government agencies shall make a good faith search of Missouri companies that provide Missouri manufactured products or services.
8. Upon request of the Missouri company, the state department for which the contract was awarded shall prepare a written explanation within 20 days of the award explaining why the Missouri manufacturer or service provider did not receive the award. This will enable Missouri companies to improve their products and services to meet Missouri government's needs and make them more competitive in the global marketplace.
9. This requirement for the purchase of Missouri products and services will become effective for all affected purchases made after December 9, 2003.

IN WITNESS WHEREOF, I have hereunto set my hand and caused to be affixed the Great Seal of the State of Missouri, in the City of Jefferson on this 2nd day of December, 2003.

**MISSOURI FIRST EXECUTIVE ORDER REQUIREMENTS AND MATRIX**

**Definition of Missouri Product:** goods or commodities, which are manufactured, mined, produced or grown by companies in Missouri, or services provided by such companies in Missouri. OA/PMM<sup>1</sup> has determined that if the company has a presence in Missouri, they will be treated as a Missouri firm. Presence must be an actual office or location operating in the state but does not mandate a headquarters operating in Missouri.

**Definition of Lowest and Best:** an award decision made by the government where cost and other factors are considered in the evaluation process. Methods include: low bid meeting specifications/requirements; qualified products list; low bid with no bad references; subjective criteria bids using value, performance and quality of product (subjective criteria weights must be stipulated in the solicitation document).

**Executive Order Requirements:**

1. Agencies shall purchase a Missouri product unless it is determined that the value (including, but not limited to price, performance and quality) of the Missouri product does not meet the needs of the user.
  - a. Local delegation: Agencies must properly document the need of the items and requirements being purchased. Statutes require competitive bids on purchases in excess of \$3,000.00. Missouri products/services must be purchased unless it is determined that the value (including, but not limited to price, performance and quality) of the Missouri product/service does not meet the needs of the user. Competitive bids using subjective criteria under the local delegation may utilize the method described by the DPMM and evaluate economic impact as described in this document.
  - b. PMM Procurements: The Division of Purchasing and Materials Management has developed a matrix that will be used to determine Missouri First Executive Order opportunities. The matrix is attached to this document.
2. The Commissioner and other agencies may consider the economic impact to the State of Missouri for Missouri products versus the economic impact of products generated from out of state. This economic impact may include the revenues returned to the state through tax revenue obligations.
  - a. OA/PMM will not implement a preference policy that would affect Missouri product/service providers doing business with other state governments similar to Missouri statute 34.076. Therefore, there will be no specific preference given for Missouri products.

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<sup>1</sup>OA used PMM and DPMM in lieu of the Division of Purchasing and Materials Management.

## APPENDIX IV

- b. OA/PMM will utilize subjective criteria functionality, to implement economic impact considerations by incorporating the following questions in Scope of Work, Contractor Support, or pertinent sections of the evaluative criteria.
    - 1. Provide a description of the proposed services that will be performed and/or the proposed products that will be provided by Missourians and/or Missouri products.
    - 2. Provide a description of the economic impact returned to the State of Missouri through tax revenue obligations.
    - 3. Provide a description of the company's economic presence within the State of Missouri (e.g., type of facilities: sales offices; sales outlets; divisions; manufacturing; warehouse; other), including Missouri employee statistics.
  - c. The evaluator or evaluation committee shall consider the economic impact in the overall subjective evaluation of the criteria.
3. The Commissioner of Administration shall make efforts to identify and give notice of state government bidding opportunities to Missouri Manufacturers or service providers. The Commissioner shall provide a listing of Missouri products and access to such listing to all state government and other interested parties. The Commissioner shall ensure state agencies follow the requirements of the Buy Missouri Products First Executive Order.
- a. OA/PMM currently places notice on its website for all procurements issued by this office. We have also included bids by the Department of Revenue on our site. In addition, we have provided links to other agency bid sites. Agencies must submit links of potential bid opportunities so we may post on OA/PMM's web site. In addition, it is the responsibility of the agency to ensure bidding opportunities are made available to Missouri manufacturers or service providers for procurements under their delegation of authority.
  - b. OA/PMM will provide a listing showing Internet links of organizations representing Missouri manufacturers and service providers on its website. A section under "Show Me" will identify "where to find Missouri product and service providers". This link will take the user to a screen identifying links identifying the above. This site shall not be used to identify individual companies. It is intended only to provide notice of organizations representing Missouri manufacturers and service providers.
  - c. OA/PMM shall incorporate the Buy Missouri Products First Executive Order requirements in its delegation of authority. In addition, the OA/PMM shall review agency performance in its procurement audits (dependent upon resource availability).



## APPENDIX IV

4. State government agencies shall make a good faith search of Missouri companies that provide Missouri Manufactured products or services.
  - a. Missouri vendors must be used if sources available to serve the needs of the agency.
  - b. OA/DPMM will provide website links to organizations of Missouri manufacturers and service providers.
5. Upon request of the Missouri Company, the agency shall prepare a written explanation within 20 days of the award explaining why the Missouri manufacturer or service provider did not receive the award.
  - a. The open records statute identifies that all records must be made available to the public. (RFQ/IFB upon opening date; RFP upon award).<sup>2</sup>
  - b. For bids awarded via low bid meeting specification, the abstract of responses (must include determination of responsiveness) shall be used as an explanation of the award decision.
  - c. For bids awarded via subjective evaluation, the evaluation report shall be used as an explanation of the award decision.

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<sup>2</sup>RFQ/IFB/RFP refers to request for quote, invitation for bid, and request for proposal.

**OFFICE OF ADMINISTRATION DECISION MATRIX**